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SUBJECT: SERBIA: DELTA REAL ESTATE'S LOFTY PLANS TEMPERED BY
FINANCIAL CRISIS

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SUMMARY

1. (SBU) In October 2008, Delta Holdings, owned by controversial Serbian billionaire Miroslav Miskovic, opened the region's second modern shopping mall in Montenegro with high level government officials and business elite from Serbia and neighboring countries in attendance. Just a year after the first modern mall opened in Belgrade, Delta wanted to give attendees a taste of its plans to expand operations in the region. Recently however, Delta's expansion plans have been tempered amid the current financial crisis. Delta's real estate arm has put projects on hold and is considering selling properties in response to the tightening of investors' purse strings. End Summary.

Delta's Mega Mall Entry

2. (U) In October 2008, Delta City Podgorica opened to remarkable fanfare. In attendance at Montenegro's first modern shopping mall opening was Montenegrin PM Milo Djukanovic, Serbian PM Mirko Cvetkovic, Republika Srpska Premier Milorad Dodik, Skopje mayor Trifun Kostovski, Ljubljana mayor Zoran Jankovic and regional business elites. Many of these well-to-dos were flown in via charter flight courtesy of Delta Holdings (Delta) owner Miroslav Miskovic (reftel). Delta City Podgorica opened almost a year after Delta City Belgrade, the region's first modern shopping mall (standing in the middle of Delta City you might never realize you were not in the Pentagon City mall). The spectacular grand opening was one of several Delta Real Estate (DRE)-the division that develops shopping malls, retail parks, and mixed-residential buildings - is planning in the region and in Serbia. DRE currently owns land in Serbia, Montenegro, Slovenia, and Bosnia and Herzegovina and plans to buy property in Albania, Macedonia, and Croatia.

Regional Expansion and Reception

3. (SBU) Miskovic openly supports Serbian accession to the EU and investment opportunities in the region as evidenced by the October 20 meeting in Brussels that Delta co-sponsored. At the meeting of Serbian businessmen, EU Enlargement Commissioner Olli Rehn, EU representatives and international banks, Miskovic pointed out trade and investment impediments he believed were due to "interference of daily politics." In a meeting with us on November 12, DRE CEO Dejan Racic said neighboring countries "have reservations about Serbia" when asked about the reception Delta receives in neighboring markets. In Montenegro and Republika Srpska (RS) Delta seems to be well-received. Miskovic opened a Tempo supermarket in Banja Luka in September 2008 with Premier Dodik in attendance and later announced Delta's goal to control 40% of the RS retail market. In Sarajevo, however, Delta's purported partnership with Fahrudin Radoncic, the

owner of the Dnevni Avaz newspaper and many real estate properties has been more controversial.

¶4. (SBU) In August 2008, DRE signed an agreement with Slovenian firm Grep to build a sports park that will house the Delta Planet shopping center, a stadium, and a sports hall. In October 2008, Delta announced plans to buy the Slovenian retail chain Mercator. Soon after, however, the Slovene government said it would take "unprecedented measures in the sale of Mercator," amid concerns that foreign ownership would threaten the Slovenian food industry. In Bulgaria, Delta bought 85 percent of supermarket chain Piccadilly in October 2007, the first significant Serbian capital investment in an EU country. Two Piccadilly stores later suffered explosions in August 2008 which some media speculated were a message to Miskovic. Racic said that even though Delta planned to expand to Croatia, he knew that Serbian businesses (and Serbs) were not welcomed in many Croatian cities; therefore DRE would likely enter the market with a local partner.

At Home in Serbia

¶5. (U) In Serbia, DRE also has sizable development plans. In a joint venture with Hypo Bank, DRE is building residential and commercial spaces for the 2009 University Games hosted in Belgrade. Racic said almost all of the University Games units have been pre-sold, with 60% of buyers paying with cash. Racic outlined his plan to build a Crown Plaza Hotel and luxury apartment office spaces on land DRE acquired in a tender earlier this year. Other plans include shopping centers in Kragujevac and Novi Sad.

Tempered Expectations Amid Financial Crisis

¶6. (SBU) Although DRE has lofty plans, the current financial crisis has recently tempered its short term expectations. DRE is actively seeking international project financing and partners, but Racic said potential investors were not panning out as liquidity and credit availability had dried up. In response, Racic said DRE would likely have to sell some of its undeveloped land purchased on credit, mainly in Serbia, to reduce its debt burden. He insisted that there was still a "huge potential" for commercial real estate, particularly in upscale, premium office space, but demand remained cyclical. Racic added that the housing market was not overblown in Serbia. In a conversation with us on October 1, Colliers International Senior Consultant Bosko Tomasevic was optimistic about Serbia's real estate market saying there was continued demand for residential property especially in Belgrade where demand outweighed supply considerably. He added that DRE was "growing fast" and aggressively recruiting young talent from abroad and from Colliers.

¶7. (SBU) On December 1, Merrill Lynch's Director of Global Principal Investments Rob Schweizer told us that he believed land prices would go down, but that the pent-up demand for affordable residential property in Serbia would continue for the next 10 to 15 years. Merrill invested in DRE competitor MPC properties in late 2007. He added that companies like DRE that built high-end apartments and depended on large investments from abroad would suffer as euro and dollar-based investors could not "rationalize investing in Serbia when they can get the same and more secure return in Western Europe." Schweizer said DRE made "emotional investments," often buying land with no money or plans to develop it, which was why DRE has had to scale back on several plans.

¶8. (SBU) Vladimir Mrvic, former Chairman of the Board of Hypo Bank Consultants and current CEO of Capital Consultants, said in a meeting with us on October 3 that DRE's financing difficulties were well known and that several of Mrvic's Israeli clients had expressed interest in Serbian real estate, but were too "scared" to invest at this time. As a real estate consultant (and also one of those flown in for the Delta City Podgorica opening), Mrvic followed Delta and DRE projects closely and commented that among his business circle, the "corruption feeling" that had long been associated with Miskovic and Delta had lessened recently as Miskovic seemed to be adamant about maintaining "clean" and legal accounting.

COMMENT

19. (SBU) In the current economic environment, even the country's largest developer has not convinced new real estate investors to come to Serbia. DRE met with a string of U.S. equity funds over the past year in search of an equity partner to support DRE's growth and development plans. To date, DRE has been unsuccessful, despite high-level discussions with at least three major international equity firms. The firms that have discussed some of their internal decision making with the Embassy have told us that DRE was professionally run, but they remained concerned about the unknown risks of Miskovic's controversial image. Serbia, and in particular Belgrade, still suffers from a shortage of residential housing which keeps its real estate prices on par with those of many Western European countries, and is a source of constant aggravation to the middle class. Miskovic remains a controversial figure, who despite his successful businesses has been unable to change his reputation and image. If the market had robust growth and bright near-term prospects DRE might have been successful in finding investment from sources willing to accept some additional risks. However, in today's market DRE faces a difficult road in Serbia, and also in pursuing it. End Comment.

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MUNTER